



year ended june 30, 2001

Operations Summary

California Public Employees' Retirement System

CalPERS

70
years of service



CalPERS Profile

The California Public Employees' Retirement System (CalPERS) is the nation's largest public pension fund and the second largest in the world, with assets at June 30, 2001 of approximately \$156 billion.

Headquartered in Sacramento, CalPERS provides retirement and health benefit services to nearly 1.3 million people and more than 2,400 public employers. The System also operates eight regional offices located in San Francisco, Glendale, Orange County, Sacramento, San Bernardino, San Diego, Mountain View, and Fresno.

CalPERS is led by a 13-member Board of Administration, consisting of member-elected, appointed, and ex officio members.

Our membership consists of 916,632 active and inactive members from the State, school districts, and local public agencies, and 369,278 retirees, beneficiaries, and survivors. Established by legislation in 1931, the System became operational in 1932 for State employees only. In 1939, public agencies were allowed to contract with CalPERS to provide retirement benefits for their employees. We began administering health benefits to State employees in 1962 under the Public Employees' Medical and Hospital Care Act. Local public agencies joined in our health program on a contract basis five years later.

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year ended june 30, 2001

Operations Summary

California Public Employees' Retirement System

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Operations Summary

PUBLIC EMPLOYEES' RETIREMENT FUND¹

(Dollars in Thousands)

	2001	2000
Assets		
Cash & Cash Equivalents	\$25,127	\$9,848
Investments, at Fair Value	170,137,409	188,062,022
Receivables	3,458,569	3,004,709
Other Assets	95,611	80,733
Total Assets	\$173,716,716	\$191,157,312
Liabilities	\$17,442,319	\$18,616,768
Net Assets Held in Trust for Pension Benefits	\$156,274,397	\$172,540,544

ADDITIONS & DEDUCTIONS

	2001	2000
Additions		
Member Contributions	\$1,766,256	\$1,751,290
Employer Contributions	321,619	362,614
Net Investments Income	(12,255,822)	16,579,088
Other	7,481	3,570
Total Additions	(\$10,160,466)	\$18,696,562
Deductions		
Retirement, Death & Survivor Benefits	\$5,792,949	\$5,176,073
Refunds	128,866	140,644
Administrative Costs	183,866	175,051
Total Deductions	\$6,105,681	\$5,491,768
Increase in Net Assets Held in Trust for Pension Benefits	(\$16,266,147)	\$13,204,794
Transfer to Supplemental Contributions Program Fund	\$ —	(\$22,035)
Change in Net Assets Held in Trust for Pension Benefits	(\$16,266,147)	\$13,182,759

Complete financial information of all the Funds administered by CalPERS can be found in the Comprehensive Annual Financial Report for the year ended June 30, 2001.

NOTE:

¹ Differences in the amount shown for investment assets in these Financial Highlights and the Investment Portfolio amount reported in the Investments Section of this summary are due to differences in reporting methods. In accordance with GASB Statement No. 28, financial statements include Securities Lending Collateral. Also, Net Investment Receivables/Payables are not included here.

Dear Friends:

It is an honor, during this, the 70th anniversary of our founding, to present the CalPERS Operations Summary and Comprehensive Annual Financial Report for the fiscal year ended June 30, 2001.

On June 9, 1931, the Governor signed the law that directed the establishment of the State Retirement System. We opened our doors the following January.



Dr. William Dale Crist
President

The world is a far different place now than it was when the need for a public employees' retirement system in California was first envisioned. But our efforts to advance the retirement security of all our members are as important today as in 1931. Other mandates have been added along the way, such as our responsibility to advance the health security of our members, but the basic mission of protecting members' financial security remains the same.

We are careful to keep the long-range view clearly in sight, especially during turbulent economic and political times. Fiscal year 2000-01 included such challenges as a roller coaster stock market, a hostile health care market, a threatening energy shortage, and an overall weakened economy.

Indeed, it was not a good year for growth in assets anywhere, and CalPERS was not spared. Our assets stood at approximately \$156 billion on June 30, 2001, a 7.2 percent investment loss from the previous year. This loss was caused by the significant decline in public equity markets around the world. But, even with this lackluster investment year, our long-term investment returns remain solid and positive, earning a 10.6 percent return over the past five years and 11.4 percent over the last 10 years.

In our health benefits program, we worked very hard on behalf of our members to obtain affordable, quality health benefits. We brought financial stability to our self-funded preferred provider organizations (PERSCare and PERS Choice), which were experiencing unparalleled member growth, higher utilization, and higher medical costs. The unpleasant task of increasing some member copayments in both our self-funded plans and for members of health maintenance organizations is helping us stem the tide of out-of-control prescription drug costs. This year we pushed negotiating with our contracting health plans to the limit, rejecting all initial bids, and settling only with those plans that offered the best quality at an affordable price.

In the customer service arena, we are proud to say we have substantially reduced telephone waiting times, and members can now reach our Regional Offices through one single phone number. In addition, we joined the higher-tech world with our launch of a “self-service” system on the CalPERS web site. Today, members can view personal data on their Annual Member Statement on-line and use that data to develop an on-line retirement estimate. More beneficial uses of the Internet are being planned.

We have made great strides in improving service to employers as well. More and more employers are now using our Automated Communications Exchange System. Contract amendments are handled more quickly than ever before, and valuations continue to be provided to agencies in a timely fashion.

As we look toward fiscal year 2001-02, we know we will continue to experience severe challenges in the investment market and the health benefit purchasing arena. We will remain steadfast in our commitment to do our very best, remembering that our success in dealing with immediate challenges is critical to the quality of life for CalPERS members—now and in the distant future. You can expect us to continue our drive toward improving the quality of service provided by CalPERS. And we will, as always, be guided by the needs of our members and employers.

Respectfully submitted,



William Dale Crist, President
CalPERS Board of Administration

Board of Administration

William Dale Crist, President

*Employee Member (elected by State members)
Professor, CSU Stanislaus
Term Ends: January 15, 2003*

Robert F. Carlson, Vice President

*Retired Member (elected by retirees)
Retired—Chief Counsel, Department
of Transportation
Term Ends: January 15, 2004*

Sidney L. Abrams

*Official of Life Insurer¹
Trustee, United Food and Commercial Workers
Unions and Employers Midwest Health Benefits
Fund and Pension Fund
Term Ends: January 15, 2005*

Philip Angelides

*State Treasurer
Ex Officio Member*

Willie L. Brown, Jr.

*Elected Official of Local Government¹
Mayor of San Francisco
Term Ends: January 15, 2004*

Kathleen Connell

*State Controller
Ex Officio Member*



CalPERS BOARD OF ADMINISTRATION

(back row to front row, left to right):

Kathleen Connell, Charles P. Valdes, Willie L. Brown, Jr., Sean Harrigan,
Rob Feckner, Jennifer Ducray-Morrill (representative for Philip Angelides),
Sidney L. Abrams, Marty Morgenstern, Mike Quevedo, Jr., William Rosenberg,
William Dale Crist, Robert F. Carlson, Michael Flaherman

Rob Feckner

*Employee Member (elected by school members)
Glazing Specialist, Napa Valley Unified
School District
Term Ends: January 15, 2003*

Michael Flaherman

*Employee Member (elected by public
agency members)
Economist, Bay Area Rapid Transit
Term Ends: January 15, 2003*

Sean Harrigan

*State Personnel Board Member (designated by
the State Personnel Board)
Term Ends: Serves at the pleasure of the State
Personnel Board*

Marty Morgenstern

*Director, Department of Personnel
Administration
Ex Officio Member*

Mike Quevedo, Jr.

*Public Representative ²
Term Ends: January 15, 2004*

William Rosenberg

*Employee Member (elected by all members)
Retired—Retirement Specialist, CalPERS
Term Ends: January 15, 2002*

Charles P. Valdes

*Employee Member (elected by all members)
Counsel, Department of Transportation
Term Ends: January 15, 2002 ³*

NOTES:

¹ Governor appointee.

² Appointed jointly by the Speaker of the Assembly and the Senate Rules Committee.

³ Mr. Valdes was re-elected in November 2001. His new term begins January 15, 2002 and ends January 15, 2006.

In addition to their regular duties, Board Members also serve on permanent and ad hoc committees to review specific programs, projects, or issues and make recommendations to the Board. The following committees were active as of June 30, 2001.

Benefits & Program Administration

Rob Feckner, Chair
William Rosenberg, Vice Chair

Sidney L. Abrams
Robert F. Carlson
Kathleen Connell
William D. Crist
Michael Flaherman
Sean Harrigan
Marty Morgenstern

This committee reviews all matters related to benefit program structure, actuarial studies and rate setting, retirement program policy, and administrative issues.

Health Benefits

Rob Feckner, Chair
William Rosenberg, Vice Chair

Sidney L. Abrams
Philip Angelides
Kathleen Connell
Sean Harrigan
Marty Morgenstern
Charles P. Valdes

This committee oversees the administration of the Public Employees' Medical & Hospital Care Act program and the Public Employees' Long-Term Care Act program.

Finance

Robert F. Carlson, Chair
Kathleen Connell, Vice Chair

Philip Angelides
William D. Crist
Michael Flaherman
William Rosenberg
Charles P. Valdes

This committee provides financial oversight on all budget matters, evaluates funding alternatives, oversees preparation and recommends approval of the CalPERS budget, and oversees the CalPERS annual and periodic audits by both internal and external audit units.

Performance & Compensation

Charles P. Valdes, Chair
Robert F. Carlson, Vice Chair

William D. Crist
Rob Feckner
Michael Flaherman

This committee studies and evaluates compensation mechanisms and criteria, develops policies and procedures, and makes recommendations to the Board concerning compensation of key personnel.

Investment

Michael Flaherman, Chair

Sean Harrigan, Vice Chair

Sidney L. Abrams

Philip Angelides

Willie L. Brown, Jr.

Robert F. Carlson

Kathleen Connell

William D. Crist

Rob Feckner

Marty Morgenstern

Mike Quevedo, Jr.

William Rosenberg

Charles P. Valdes

This committee reviews investment transactions, the investment performance of both internal and external managers, and establishes investment policy and strategy.

Ad Hoc Internal Board Governance

Review Committee

Sean Harrigan, Chair

Michael Flaherman, Vice Chair

Robert F. Carlson

Rob Feckner

William Rosenberg

Charles P. Valdes

This ad hoc committee reviews all of the CalPERS internal Board governance policies and processes and makes recommendations for improvements to the Board of Administration.

Investment Policy Subcommittee

Charles P. Valdes, Chair

Philip Angelides, Vice Chair

Robert F. Carlson

This subcommittee conducts an inventory of all existing investment policies, procedures, and guidelines for review by the Investment Committee and reviews and recommends revisions to these on a priority basis. It is also charged with developing a manual of policies, procedures, and guidelines, and a process for periodic revisions.

R Street Subcommittee

Charles P. Valdes, Chair

Robert F. Carlson, Vice Chair

William D. Crist

Rob Feckner

Michael Flaherman

This subcommittee oversees the CalPERS headquarters expansion project, including the selection of contractors, approval of building designs, and approval of expenditures and budgets.

Executive Staff

James E. Burton

Chief Executive Officer

James H. Gomez

Deputy Executive Officer

Robert Aguallo

*Assistant Executive Officer
Investment Office*

Vincent P. Brown

*Assistant Executive Officer
Financial & Administrative Services*

Allen D. Feezor

*Assistant Executive Officer
Health Benefit Services*

Kayla J. Gillan

General Counsel

Barbara Hegdal

*Assistant Executive Officer
Member & Benefit Services*

Patricia K. Macht

*Chief
Office of Public Affairs*

Ron Seeling

*Chief Actuary
Actuarial & Employer Services*

Daniel Szente

*Chief Investment Officer
Investment Office*

Robert D. Walton

*Assistant Executive Officer
Governmental Affairs, Planning & Research*



CalPERS EXECUTIVE STAFF

(back row to front row, left to right):

Patricia Macht, Robert Walton, Ron Seeling, Robert Aguallo,
Barbara Hegdal, James Burton, Allen Feezor, Daniel Szente,
Vincent Brown, James Gomez, Kayla Gillan

CalPERS
Divisions

Denise Arend

Chief, Investment Operations

Tom Britting

Chief, Office of Audit Services

Ralph Cobb

Acting Chief, Self-Funded Programs

Jack Corrie

Chief, Information Technology Services

Tom Fischer

Chief, Health Benefit Services

Tim Garza

Chief, Management Information Systems

Allen Goldstein

Chief, Change Management

Pat Harris

Chief, Branch Development Center

Linda Hoff

Chief, Office of Policy & Program Development

Charles Hwu

Administrator, Data Administration

Michael W. Koester

Chief, Operations Support Services

John Korach

Chief, Fiscal Services

Ron Kraft

Chief, Member Benefit Contact Center Division

Jeff Lung

Information Security Officer

Ken Marzion

Chief, Actuarial & Employer Services

Peter Mixon

Deputy General Counsel, Legal Office

Dave Mullins

Chief, Supplemental Savings Program

Chris Nishioka

Chief, Benefit Services

Michael Ogata

Chief, Planning & Research

Tom Pettey

Chief, Human Resources

Diana Proctor

Chief, Headquarters Expansion Project

Janet Toney

Acting Project Director, COMET

Kathy Vaughn

Chief, Member Services

Nancy Welsh

Chief, Health Program Development

Casey Young

Chief, Office of Governmental Affairs

CalPERS
Regional Offices

Anita Commer

Manager, San Francisco

June Copple

Manager, San Bernardino

Laura Duran

Manager, Orange County

Elaine Edwards

Manager, San Diego

Debra Gibson

Manager, Sacramento

Edith Mercer

Manager, Glendale

Elwin Nash

Manager, Mountain View

Steve Pietrowski

Manager, Fresno

The CalPERS mission is to advance the retirement and health security of all our members. During challenging economic times like that of fiscal year 2000-01, we are reminded of the seriousness of our purpose. We faced twin economic challenges this past year: escalating health care costs and an asset management climate affected by the downturn in the U.S. stock market. We met these challenges head on, ensuring through our short-term tactical plans and long-range strategies that retirement and health security for our members was not compromised.

During the year, we focused sharply on the day-to-day management of our retirement, health, and other supplemental benefit programs.

We also vastly expanded our ability to communicate with our members and employers.

In addition, we broadened education and training for employers.

Improving Customer Service

CalPERS has ambitious goals for improving the timeliness and quality of our customer service. We recognize that our members and employers want to have multiple ways of conducting business with us—in person, over the telephone, and through the Internet. Many of our projects this past year have focused on communication.

Telephone Customer Service

In order to make contacting CalPERS as convenient as possible, we created the Member Benefit Contact Center (MBCC). And, with an eye toward answering calls faster, the MBCC increased staffing levels during peak call volume periods. This change resulted in a more than 94 percent answer rate, up from 74 percent. In the health phone service area, we turned 20-minute wait periods into almost no waiting at all. We now have the capability to handle 100 percent of all calls within a short time frame. Together, the MBCC and our Health Benefit Services Telephone Information Center fielded nearly one million telephone calls during the year. Our goal is to eventually consolidate the retirement and health benefits telephone systems to enable members to get all their questions answered with a single call.

We also established one toll-free telephone number to contact CalPERS Regional Offices located throughout the State. Now, no matter where a member is calling from, they will be connected with the next available Regional Office representative.

Improving Customer Service Via the Web

For many years, CalPERS members have received their Annual Member Statement each October through the mail. In today's information age, however, members have become accustomed to conducting their business via the Internet. It is common today for many to go on-line to access bank accounts, order merchandise, and even track a package toward its destination. With this trend in mind, in fiscal year 2000-01, CalPERS created a new self-service gateway, ***PERSONal Access***, that allows members to use a Personal Identification Number (PIN) to access their member data in a secure environment. Active and inactive members can now use their PIN to view their Annual Member Statement. During the year, more than 10,000 PINs were issued. And a number of ***additional*** self-serve functions are planned for the coming fiscal year.

CalPERS is undergoing a revamping of our web site to make it more efficient and effective for users, and to enable members,

employers, and other stakeholders to more quickly reach the information pertinent to them. Even more steps toward making the site accessible will be introduced in fiscal year 2001-02.

retirement program

Highlights 2001

- 916,632 active & inactive members
- 369,278 retirees, beneficiaries, & survivors
- 22,147 new retirees
- \$5.8 billion paid in benefits
- 2,482 public agency employers (including school districts)

a d e r s h i p



Benefits Management & Retirement Services

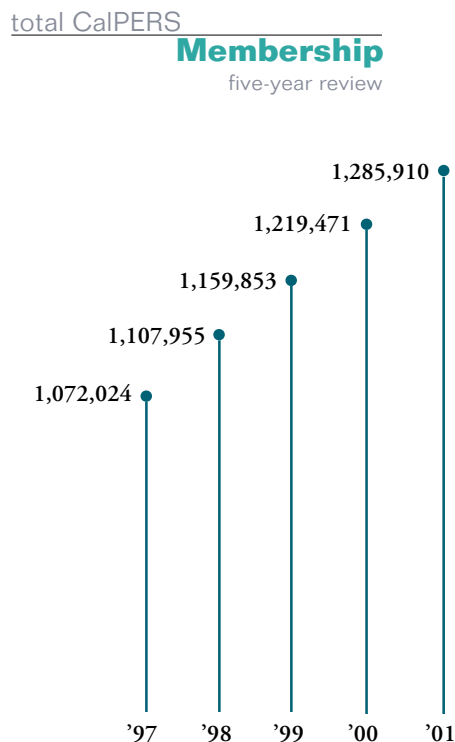
The single most-requested service in the CalPERS retirement administration arena is a retirement estimate. For several years, CalPERS has had an on-line Retirement Planning Calculator enabling members to develop their own *informal* estimate. This past fiscal year, we took that service to new heights—the Calculator was “enhanced” and made available on-line through *PERSONal Access* to allow members with PINs to have their personal and employment data *automatically* inserted from their Annual Member Statement.

Until recently, providing members a *formal* retirement estimate generally took four to six weeks. With the advent of a special project CalPERS continued this year—

the Service Level Improvement Project (SLIP)—80 percent of formal estimates are now completed in just five days and 100 percent within 30 days. SLIP also has expedited the retirement application process. With the exception of the more complex cases, such as those dealing with community property issues, 100 percent of members are placed on our retirement rolls within 30 days, up from 80 percent last fiscal year. The processing of requests for service credit purchase was also expedited.

Staff processed 19,432 new service retirements and 2,715 disability retirements during fiscal year 2000-01, and paid out approximately \$5.8 billion in retirement, death, and survivor benefits. Ninety-five percent of our newly retired members were paid within 30 days of their retirement date. In addition, we processed 27,000 refunds—99.7 percent within 30 days. Some 95 percent of pre-retirement death benefits were paid within 45 days of receipt of all required documents, and 90 percent of post-retirement death benefits were paid within 30 days of receipt of documents. Staff also completed 3,965 disability determinations.

We are particularly proud of the fact that we mailed over 45,000 election packets to State members who have State Second Tier service, allowing them to elect the First Tier using two methods formerly not available: paying over a 180-month period or taking an actuarial equivalent reduction at retirement.



CalPERS Supplemental Savings Programs

The Public Agency 457 Deferred Compensation Program welcomed 47 new public agencies and enrolled nearly 3,000 new participants, with the 10,000th participant joining in May 2001. In addition, contributions and transfers into the program increased by 50 percent.

CalPERS was successful in retaining investment management over three State Savings Plus Program funds totaling nearly \$1 billion. We also enhanced the Supplemental Contributions Program by adding quarterly valuations of the fund and crediting earnings quarterly to participant accounts. The Program operates as an independent defined contribution plan to which eligible State employees may voluntarily elect to contribute after-tax dollars.

Assets in the State Peace Officers' and Firefighters' Defined Contribution Plan increased by more than 50 percent. The Plan provides an employer-paid retirement benefit to supplement the benefits received through regular CalPERS retirement.

Member Home Loan Program

The CalPERS Member Home Loan Program, administered by more than 70 lending institutions with nearly 800 branch locations throughout the State and nationwide, offers real estate financing to our members. The program offers competitive rates, a free

60-day interest rate lock, controlled closing costs, and a 100 percent financing option (a combination of a mortgage loan and a personal loan secured against the member's contributions). During fiscal year 2000-01, the Program made 11,190 real estate loans and 2,473 personal loans, valued at approximately \$1.77 billion and \$18.7 million, respectively. This was the largest volume of real estate and personal loans issued in a single fiscal year since the inception of the program.

Member Communication and Education

Our quarterly newsletter, *PERSpective*, continues to be an extremely effective means of communicating with our members. In addition, our second annual Retirement Planning Month campaign—"Your Future. Your Choice"—was again well-received. Two new retirement planning kits and a variety of web tools were developed for the campaign, and a special edition of the CalPERS Member Network video was produced. Some 7,229 kits were mailed in response to coupons from the spring issue of *PERSpective* and from promotional posters sent to employers Statewide. During the month, nearly 9,000 hits were received on the special retirement planning pages of our web site. In addition, on May 10 an estimated 1,500 members came to the Retirement Planning Fair at the State Capitol to gather informational material and speak with retirement specialists and representatives of our various programs.

To help educate our members, we conducted 2,822 financial and retirement planning workshops and other meetings throughout the year. In addition, we produced six member education videos and released them Statewide to employers, employee organizations, and members requesting copies.

Assisting Employers

About 500 employer representatives attended the first annual CalPERS Employer Conference, themed “Working for You,” October 30-November 1, 2000 in Anaheim. Various sessions presented up-to-date information on benefit improvements, legislation, investments, customer service, current CalPERS projects, and new programs under consideration. Our latest technological advances were exhibited in the conference Technology Center, a hands-on computer lab. A special workshop also gave employers the opportunity to provide feedback to CalPERS on retirement issues important from the employer perspective.

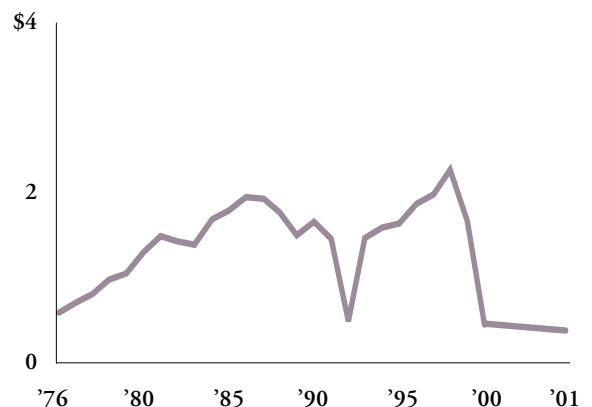
Implementation of the Automated Communications Exchange System (ACES) highlighted another notable employer service improvement this year. ACES allows employers to electronically submit retirement and health enrollments and payroll data to CalPERS through a secure Internet connection. In October 2000, an ACES web site was launched that provides information about program functions, an employer

readiness assessment, frequently asked questions, user guides, and registration instructions. A special ACES Customer Support Line was also implemented, with representatives available during business hours to troubleshoot and assist employers with accessing and navigating ACES. Some 275 employers were added to ACES during the fiscal year, and additional employers will be enrolled during the second rollout in fiscal year 2001-02.

CalPERS staff completed more than 1,700 contract amendment valuations. In addition, 557 contract amendments were processed, a 60 percent increase over last year. Some 26 new public agencies contracted with CalPERS. Throughout the year, the Actuarial and Employer Services Division trained 2,000 employer representatives in membership and payroll procedures. In April and May, staff conducted 14 one-day actuarial seminars for more than 300 attendees.

CalPERS income from Employer Contributions

25-year review
(Dollars in Billions)



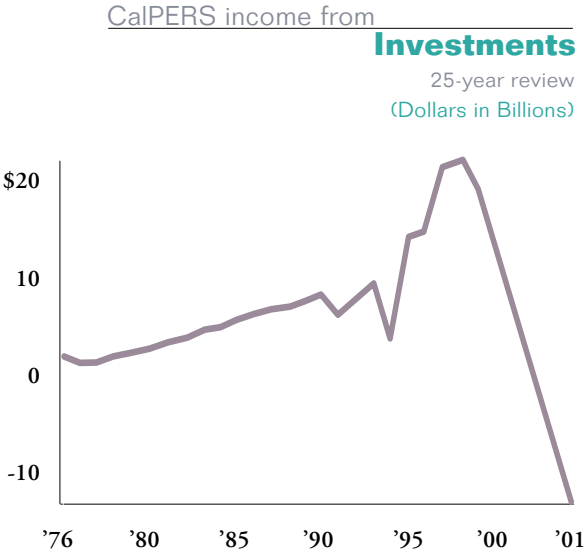
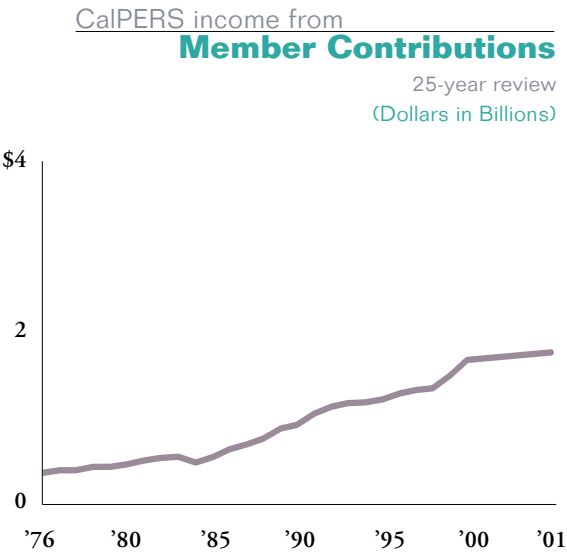
In June 2001, the CalPERS Board adopted a Benefit Equity Resolution that allows public agencies to select one of three different methods of determining the initial employer contribution rate, if they amend their contract in the 2001-02 fiscal year based on the June 30, 2000 actuarial valuation.

Organizational Effectiveness

In June 2001, the CalPERS Board approved our Three-Year Business Plan, which establishes specific business objectives aligned with each of the business goals identified in the Strategic Plan—customer service, benefits management, and asset management. Specific outcomes were also established to measure our progress. In addition, leadership and organization strategies were determined that will help us meet the needs of members, employers, and stakeholders.

During the year, CalPERS launched a Records Retention/Data Imaging Project, which will digitally store member files and allow them to be quickly and easily retrieved when needed. The initial project involves converting more than 1.4 million member files (about 48 million pages) to electronic images by July 30, 2002, after which we will explore the expansion of the project to other business records.

In other business areas, CalPERS auditors completed 44 public agency audits, 23 consulting engagements and special projects, 35 internal audit projects, 11 health plan audits, and five real estate audits. Six audit staff served as officers, committee members, or board members on the boards of various professional associations, including the Institute of Internal Auditors, American Institute of Certified Public Accountants,



Information Systems Audit and Control Association, and the Association of Public Pension Fund Auditors.

To help prepare our staff for tomorrow's demands, CalPERS launched a multi-dimensional training program via our new Learning Center, internal classes, and a new multi-tiered leadership training series.

The Learning Center offers more than 150 on-line courses that cover topics from program facilitation to customer service to computer operation, and it makes available more than 900 books, videos, and audiobooks for loan. We also instituted the KEYS (Knowledge Essential for Your Success) Program, a joint venture between CalPERS and the University of California, Davis Extension. The six core courses that comprise KEYS cover retirement planning, communication, team building, problem solving, customer service, and a unique tour of our various divisions and business functions. In addition, the new Leadership Series has training appropriate for staff at every level, from emerging leaders to seasoned veterans.

We at CalPERS also did our part during California's energy crisis by turning off escalators, dimming lights in hallways during business hours, turning off unnecessary appliances, and making sure all computers, printers, and copy machines were turned

off at the end of the workday. Through these conservation efforts, we were able to reduce our overall energy consumption during the fiscal year by approximately 11.8 percent. In our investment area, we met with all of our real estate advisors and managers to ensure that they, too, included energy conservation considerations in managing our real estate portfolio.

CalPERS each year is a source of contracts for many businesses. To ensure that our procurement processes are known to as many potential vendors as possible, in July 2000 we formed the CalPERS Business Connection, an aggressive outreach and marketing program to firms wishing to do business with CalPERS, including new, small, emerging, or disabled veteran-owned business enterprises. A business liaison was hired and an interdepartmental committee formed to help CalPERS reach mandated participation goals.

Once again CalPERS employees demonstrated their generosity by pledging nearly \$100,000 to the United California State Employees Campaign. In addition, staff donated more than \$17,000 to Daffodil Days, the March of Dimes, and Breast Cancer Awareness, and also donated 362 pints of blood. For the third year, CalPERS partnered with the Department of Corrections' Inmate Computer Refurbishing Program to donate used computers to California public schools.

Update On Our Headquarters Expansion

CalPERS has already outgrown our headquarters building, known as Lincoln Plaza. In fact, some divisions within CalPERS, including the Sacramento Regional Office, have been relocated to leased space to accommodate the growth required to keep pace with member, employer, and support services needs. To bring all our staff back to one location, the CalPERS Board agreed to build an expansion of the headquarters across the street from our existing site. During the past fiscal year, the Environmental Impact Report and building design were approved, a construction manager was selected, demolition work was completed, and soil remediation work was begun. The project has been well received by the community and the City of Sacramento. The mixed-use complex will include a building with a six-story west wing and a four-story east wing, an 18,000-square-foot public courtyard, parking for approximately 1,000 cars, retail shops and restaurants, a day-care center, and a fitness center. CalPERS plans to occupy the complex beginning in September 2004.

Honoring Employee Excellence

At a ceremony held in early November 2000, 20 CalPERS employees from throughout the State were honored with our newly created APEX award. APEX (Achieving Performance EXcellence) is the System's first peer-driven formal recognition program.

CalPERS, as a department, received various awards during the year, including a Certificate of Achievement for Excellence in Financial Reporting for our Comprehensive Annual Financial Report for the year ending June 30, 2000. This certificate is given to government agencies and public employee retirement systems whose comprehensive annual financial reports achieve the highest standards in government accounting and financial reporting. Nine awards for communication and design excellence were received from State and national public relations industry organizations. In addition, the ACES project received the "Best Solutions Award" from the Government Technology Conference 2000.

The organization was honored with the International Association of Business Communicators' EXCEL award for excellence in communications. Chief Executive Officer James E. Burton delivered an acceptance address before the 13,000-member organization of communications professionals. The award is normally given to leaders of corporations in the private sector, and it marked the first time that a public sector organization received the award.

The Health Care Dilemma: Obtaining Quality Care at Affordable Costs

The realities of spiraling costs of health care faced CalPERS in December 2000, when our two self-funded Preferred Provider Organizations (PPOs)—PERSCare and PERS Choice—were faced with low financial reserves that, if left unchecked, threatened the soundness of the \$600 million plans.

The low reserves were caused by the apparent under-pricing of the plans in previous years, an unanticipated 46 percent increase in enrollment growth, price increases by plan providers, and significant increases in use of services.

In response, the CalPERS Board adopted a financial recovery plan that combined changes in benefits, premiums, and administrative actions that were designed to make the plan financially

strong. The financial recovery package would save CalPERS \$77.9 million. It included a 5.2 percent premium adjustment in the PERSCare Basic plan; an increase of the \$500 per person deductible to \$1,000 per family; increased physician visit copayments to \$20 from a 10 percent co-insurance for PERSCare and a \$10 copayment for PERS Choice members; and a \$50 copayment for emergency room visits.

It also included the establishment of a tiered pharmacy benefit design that includes three copayment levels—one for generic drugs, a second for formulary brand-name drugs, and a third for non-formulary brand-name drugs.

The Board also adopted a 24.4 percent premium increase for PERSCare and a 16.4 percent increase for PERS Choice. Supplement to Medicare coverage for CalPERS retirees increased by 15.9 percent for members of PERSCare and 16.1 percent for PERS Choice. Most of that increase was aimed at financially stabilizing the self-funded plans, but a portion of the increase was due to implementing Assembly Bill 88, passed in 2001, which provides coverage for severe mental disorders.

HMOs Seek Historically High Premiums

The challenge of keeping costs from spiraling out of control in the self-funded plans proved to be something of a dress rehearsal when the Board began reviewing the issues related to health care costs for our Health Maintenance Organization (HMO) business in early 2001.

HMOs continued to seek double-digit premium increases, the HMO rural county exodus continued, and most HMOs ended their participation in Managed Medicare. Physician groups and hospitals continued to seek reimbursement at higher levels, and prescription drug costs rose again this past year by 10 to 15 percent. HMOs were seeking premium increases ranging from 5 percent to 41 percent.

Against this backdrop, CalPERS solicited bids from our 10 HMOs for our \$1.65 billion health care program, asking for prices on a variety of terms, all in an effort to find the very best combination of service and price.

The resulting bids were not what CalPERS expected, and, at the February 2001 Board meeting, the Board rejected them and requested the HMOs to submit new rates for 2002 that included their best bid on both a standard and alternative benefit design, with increased office visit and prescription copayments.

health program

Highlights

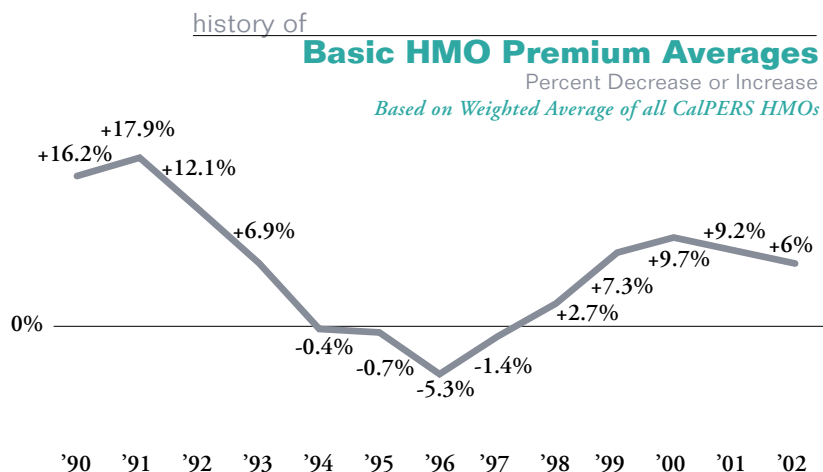
2001

- 1,204,860 employees, retirees, and family member participants
- 60 percent are State members
- 40 percent are public agency and school members
- 1,433 participating public agencies
- \$2.4 billion paid in annual health premiums
- 144,000 enrollment documents processed
- 17,749 Open Enrollment transactions completed



In April, the Board signed off on a lineup of eight HMOs, including one new entrant, a 6 percent premium increase, and a change in copayments for office visits and prescription drugs. The decision to throw out previous bids and seek new bids shaved \$176 million off the first round of bid increases. A second action by the Board to increase copayments took an additional \$134 million from the price hikes. This savings came by increasing the copayments from \$5 to \$10 per physician office visit, and replacing an existing \$5 copayment for prescription drugs with a three-tiered pharmacy benefit of \$5/\$15/\$30 and \$10/\$25/\$45, for generic, brand-name, or non-formulary brand-name drugs purchased at a retail pharmacy (30-day supply) or through the mail (90-day supply), respectively. This includes an annual out-of-pocket maximum of \$1,000 per member.

The Board accepted contracts with Blue Shield HMO, Health Plan of the Redwoods, Kaiser Permanente, Maxicare, PacificCare, Universal Care, Western Health Advantage, and Health Net. (Maxicare subsequently withdrew due to their own financial issues and later filed for bankruptcy protection.) The inclusion of Health Net was made conditional upon the completion of their professional accreditation by the National Committee on Quality Assurance (NCQA). CalPERS froze future enrollments into Health Net for its failure to meet the CalPERS requirement that HMOs be accredited by NCQA, because they broke a previous commitment to a multi-year premium rate, and for other business reasons. Even with the removal of three health plans—Aetna U.S. Health Care, Lifeguard, and Cigna—92.5 percent of members were able to continue with their primary-care physician.



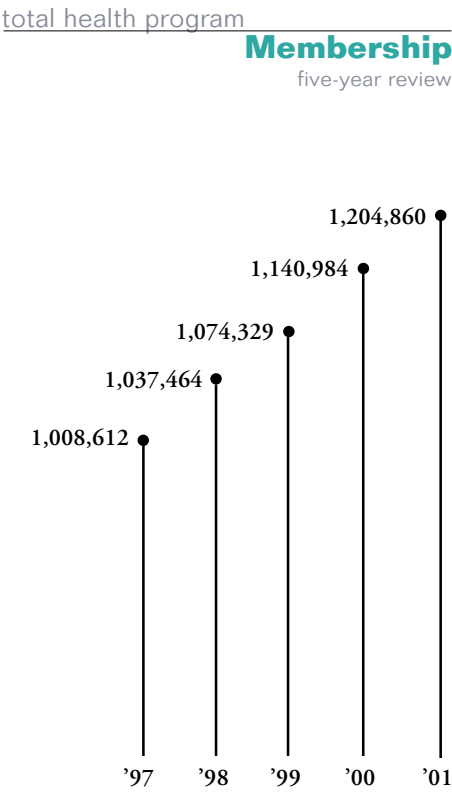
Ultimately, the 2002 health care benefits package will cost the System \$1.78 billion, compared to \$1.65 billion for 2001—the equivalent of a 6 percent Basic plan increase and a 16.5 percent Medicare plan increase. The package also creates an incentive for members to use less expensive generic drugs, and to purchase drugs by mail order, which is more economical.

Customer Service

Throughout the year, CalPERS made major progress in providing improved customer service to our members and employers. To moderate the impact of network disruptions caused when HMOs and medical providers cancel their contracts, CalPERS has included a searchable physician directory on our web site, which provides members a way to locate their current physician by health plan, specialty, geographic area, and other criteria. The directory also allows members to rate their physicians on customer service. Last year alone, this area of our site received more than 300,000 visits.

Employers have enjoyed better customer service using our Automated Communications Exchange System (ACES). Some 166 employers, covering nearly 50 percent of our health members, now use this system to register new members and change existing member data. The ANSI 834 EDI enrollment system, which is a part of ACES, was rolled out to all our health plans, speeding up the issuance of identification cards.

The 2000 Open Enrollment period was successful again this past year. Thanks to a major team effort, more than 17,749 plan changes were processed. During the entire year, an estimated 144,000 enrollments were processed—an average of 600 a day.



CalPERS once again published our Health Plan Quality Report, which helps members evaluate our HMOs and PPOs by examining patient satisfaction, access, and quality of health care. Copies of the report are available on our web site.

New Members

The Health Program grew by 5.6 percent last fiscal year, bringing the total membership to 1,204,860 active and retired public employees and their family members. In addition, a total of 1,433 agencies participate in the CalPERS health plan group, a 6.9 percent increase over the previous year. Public agencies now constitute 40 percent of our membership.

The CalPERS Long-Term Care Program

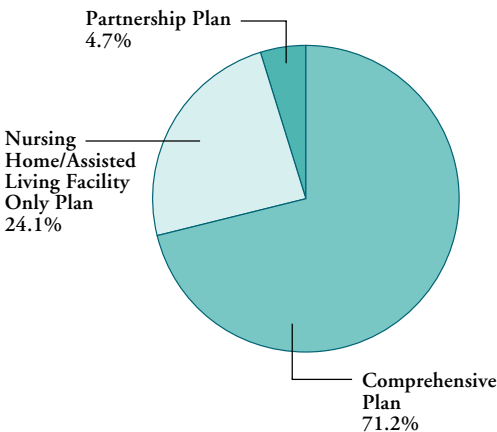
It was another year of growth for the CalPERS Long-Term Care program. At year’s end, the program was providing protection to more than 147,000 public employees, teachers, retirees, and their family members, up from 131,000 the year before. Thousands more apply each application period, and this number is expected to rise

beginning in 2002, as the result of the passage of Assembly Bill 824, which authorizes the Program to accept applications from the siblings (age 18 and older) of active and retired public employees.

Long-term care covers personal, non-medical assistance in performing ordinary activities of daily living, such as bathing, dressing, toileting, transferring (moving in and out of a bed, chair, or wheelchair), eating, and continence.

The program includes three plans: the Comprehensive plan, the Nursing Home/ Assisted Living Facility Only plan, and the Partnership plan. The Comprehensive plan covers care at home or in a community, nursing home, or assisted living facility; the Nursing Home plan covers care in a nursing home or assisted living care facility; and the

LTC membership by **Plan Type**



Partnership plan covers home, community, nursing home, and assisted living care, with a MediCal asset protection feature. Each plan includes care advisory services, respite care (to provide short-term relief to family caregivers), premium waiver while receiving benefits, portability, and guaranteed renewal from year to year.

Although many companies offer long-term care coverage, CalPERS offers the nation's first self-funded, not-for-profit long-term care program, with plans that cost significantly less than comparable commercial plans. Premiums are paid by the individual and are based on the age when the application is received. Benefits are tax-free, and premiums may be tax deductible under certain circumstances. The total coverage amount applies to all covered services, so members can use their benefits in whatever

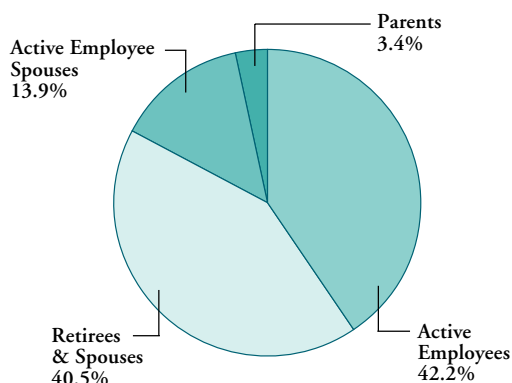
combination best meets their needs. In addition, the deductible period is counted in calendar days—not days of paid service, enabling members to save money, while staying at home.

Some 71.2 percent of all enrollees are in the Comprehensive plan; 24.1 percent are enrolled in the Nursing Home/Assisted Living Facility Only plan; and 4.7 percent are in the Partnership plan. Some 70 percent of all members opted for automatic inflation protection, and 76.8 percent chose a plan with an unlimited lifetime benefit.

During 2000-01, annual premiums stood at \$168.6 million; claims for 2001 were \$18.1 million. The average annual premium was \$1,208.

LTC program

Membership



long-term care program

Highlights

2001

- 147,169 participants
- \$1,208 is average annual premium
- \$168.6 million annual premium income
- \$18.1 million paid in claims

Long-Term Returns Remain Solid

The CalPERS investment portfolio fell back to approximately \$156 billion for the fiscal year ended June 30, 2001, a 7.2 percent investment loss attributable to lackluster global equity markets. Nevertheless, our long-term investment returns still remain solid and positive. We earned a 10.6 percent return for the five-year period ended June 30, 2001, and an 11.4 percent return for the 10-year period. Our long-term performance fared better than most multi-billion dollar public pension funds, according to data compiled by the Trust Universe Comparison Service.

Our investment portfolio remains in good shape and well ahead of where we need to be in terms of growth of assets and long-term returns, and we remain confident in our investment strategy and ability to effectively manage the System's assets in the current market environment.

Clearly, our performance for the fiscal year interjected a sense of reality into what has been a fairy-tale environment in the equity markets. Equity market returns in particular have been abnormally high in recent years, and a return to more normal conditions was expected. We have always known that we would have to give back some of our spectacular stock market returns, and we have planned for this event by maintaining a well-diversified investment portfolio.

At the end of the year, U.S. and international stock investments represented approximately 59 percent of our assets. U.S. and international bonds made up 28 percent of our investments, while real estate and private equity investments represented 8 percent and 5 percent, respectively.

Our real estate and U.S. fixed income investments showed strong gains during the year and beat industry benchmarks, which helped offset our losses in the stock market. Our real estate investments earned a 14.4 percent return for the one-year period ended June 30, compared to an 11.2 percent return for the NCREIF Index. The pension fund's U.S. fixed income assets returned 12.6 percent, beating the 11.8 percent return earned by the Salomon Brothers Large Pension Fund Index.

Our international bonds posted a 7.4 percent loss but fared better than the industry benchmark, the Salomon Brothers Non-\$ World Government Index, which suffered a 7.5 percent decline.

In the equity markets, our international stocks fell 20.1 percent, compared to a 21.8 percent loss for the benchmark.

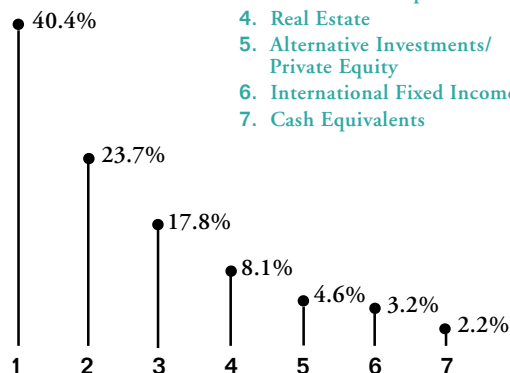
Our U.S. stocks declined by 14 percent, but still outperformed the Wilshire 2500 index, which lost 15.4 percent. Our private equity portfolio posted an 11 percent loss, below its hurdle rate, but well in line with the private equity market. According to data released by Venture Economics, private equity investments lost 11.2 percent in the first nine months of the fiscal year.

At the end of the year, we held approximately \$92 billion in U.S. and international stocks, \$44 billion in U.S. and international bonds, \$13 billion in real estate, and \$7 billion in privately held investments.

investment mix by

Asset Class

1. Domestic Equities
2. Domestic Fixed Income
3. International Equities
4. Real Estate
5. Alternative Investments/
Private Equity
6. International Fixed Income
7. Cash Equivalents



ountability

Investment Policy and Strategy

Asset allocation is one of the most important decisions made by the CalPERS Board of Administration. In the long run, it is the way in which the Board diversifies stocks, bonds, real estate, and other investments that determines the System’s long-term performance. The CalPERS asset allocation mix is decided following an extensive review of a variety of factors. Economic scenarios of the global financial markets are simulated, and future liabilities and expected future contributions by employers are considered.

CalPERS Investment Performance Goals

The Board also establishes investment policies for each portfolio and annual performance benchmarks for each asset class. Investment policies are formally reviewed through the Board’s Investment Policy Subcommittee and receive final approval by the Investment Committee.

performance

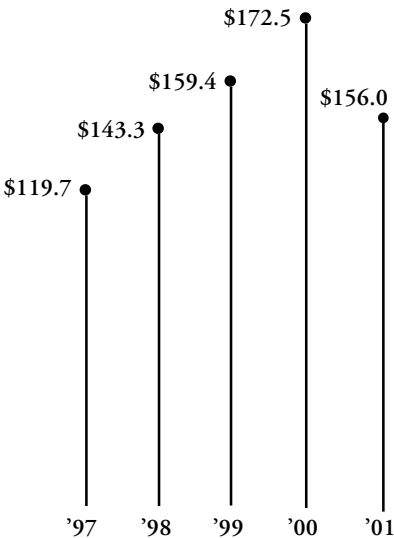
Benchmarks

Asset Class	Benchmark
Fixed Income	
Domestic	Salomon Brothers Large Pension Fund Index
International	Salomon Brothers Non-\$ World Government Index
Equities	
Domestic	Wilshire 2500 Index
International	Financial Times Actuaries/IF Investable Index
Alternative Investments	15 Percent Hurdle Rate
Real Estate	NCREIF Property Index

Alternative Investment Management

New innovative investment vehicles and relationships with top investors served as our focus during the year in our Alternative Investment Management (AIM) Program. These investments were built with a strong organizational approach to private equity investing to improve long-term risk-and-return performance. We continued to evolve the program by strengthening our relationship with our investment partners and streamlining our investment process. Our goal was to become an attractive investor and ensure that CalPERS became the “Investor of Choice.”

growth of
Investment Portfolio
Market Value
five-year review
(Dollars in Billions)



Early in the year we expanded our portfolio in the international markets and placed \$200 million in Central and Eastern Europe private equity investments. The new investments, led by leading bank and asset management groups in Central Europe, focus on regional investment opportunities in Poland, Hungary, and the Czech Republic. We invested \$150 million in Dresdner Kleinwort Benson Europe, L.P. and \$50 million in the Polish Enterprise Fund IV, L.P. We believe the economic growth in Central and Eastern Europe is a strong foundation for these investments and that the convergence of the Eastern and Western European economies has established a “Eurozone” capable of supporting a successful private equity investment program. Both funds invest in and build regional businesses and create joint ventures with major multinational corporate partners.

CalPERS continued to target direct private equity investments alongside large, sophisticated corporate partners and management teams. We invested \$425 million as part of a strategic financial relationship with The Carlyle Group, one of the world’s largest global private equity firms. We invested \$250 million in a number of new Carlyle private equity funds, purchased a minority equity stake in the firm for \$175 million, and earmarked \$425 million for future business activity of the firm.

Nearly \$1.3 billion was invested during the year in three Alternative Investment Management program innovative investment vehicles. We invested \$275 million in the biotechnology industry as part of the CalPERS California Biotechnology Fund and \$475 million in private equity investments that serve regions in California that have been overlooked by traditional capital. In addition, we earmarked \$500 million to California Emerging Ventures, our venture capital investment vehicle.

The \$275 million biotechnology investment is shared by three California-based biotech investments funds and one headquartered in New York. We made a \$100 million investment in Prospect Venture Partners II, a Palo Alto venture capital firm that focuses exclusively on life science investments; a \$100 million investment in MPM Biotech Crossover Fund, L.P., a South San Francisco fund that makes both private and public investments in the biotechnology industry;

a closer look at **AIM**
Investments & Commitments
(Dollars in Billions)

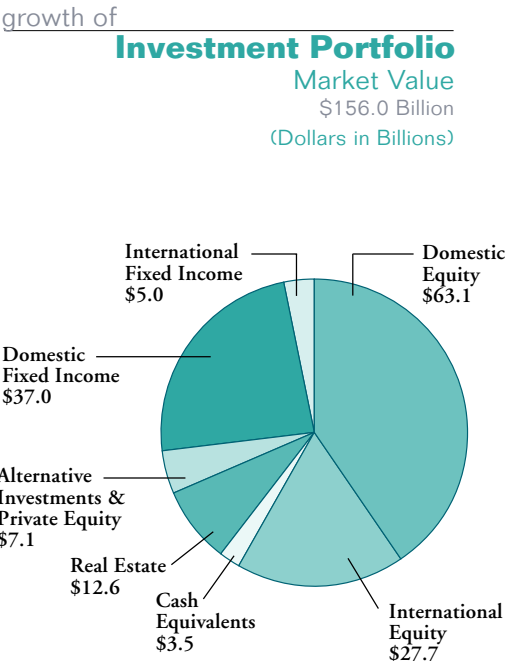
Program Types	Number of Investments	Total \$ Investment
Partnership Program	177	\$14.0
Co-Investments	16	0.4
Direct Investments	4	1.0
Investment Vehicle	7	3.8
Total	204	\$19.2

a \$25 million investment in Burrill Life Sciences Capital Partners, a fund sponsored by Burrill & Co., a San Francisco private merchant bank dedicated to life sciences through private equity investing, corporate partnering, and commercial development; and a \$50 million investment with EuclidSR, a partnership between New York-based Euclid partners and S.R. One, Limited, the venture capital arm of Smith Kline Beecham.

Our investments in the biotechnology arena are expected to help us build profitable investment relationships with large pharmaceutical companies. We believe the industry offers many compelling investment opportunities. New technologies are allowing for the development of better and more cost-effective products and drugs. These advancements, backed by CalPERS capital, can produce significant returns for the Fund while addressing unmet patient needs.

CalPERS also committed \$500 million to the venture capital industry as part of the System's California Emerging Ventures fund run by Grove Street Advisors of Wesley, Massachusetts. The investment increased our exposure to the venture capital industry to more than \$2 billion. The infusion of new capital will allow us to continue to invest with the top-tier venture capital teams through market cycles and build on the Fund's investment success. California Emerging Ventures has invested with more than 74 investment teams in the venture capital investment arena, including some rapidly emerging names such as Insight Capital Partners, Oxford BioScience Partners, and Trident Capital. Preliminary performance analysis shows that the California Emerging Ventures fund generated a gross internal rate of return of 78 percent for all its portfolio investments as of September 30, 2000.

California's underserved urban and rural markets were the recipient of \$475 million in capital from CalPERS during the year. We approved hiring 11 venture capital and private equity firms to invest in California's urban and rural communities. We believe the absence of capital in these areas provides tremendous opportunity for the Fund. Investments are regionally focused to capitalize on California's expected growth, 70 percent of which is expected to occur in urban areas surrounding Los Angeles, San Francisco, and San Diego.



The outlook of our private equity portfolio is good. We have developed a reputation as a market leader and innovator and have a diversified portfolio across stages of opportunities, industries, and geographies. While still young, the portfolio is at its prime to capture investment opportunities offered in the recent market downturn. Companies are turning to private markets for financing, and valuations are low. We are well-positioned, given that only a small portion of our investment commitments have been drawn down and invested, resulting in available capital to make new investments.

Real Estate

The purchase of high-quality real estate assets in strong markets across the country served as the primary focus of our real estate program during the year.

One of the single largest retail transactions in the U.S. led our acquisition efforts when we acquired Bethesda, Maryland-based First Washington Realty Trust, Inc. for approximately \$800 million. The investment included 63 properties totaling 6.6 million square feet of supermarket-anchored neighborhood shopping centers located in key metropolitan areas of Washington, D.C., Baltimore, Northern Virginia, Philadelphia, and Chicago. The transaction strengthened our exposure on the East Coast and enabled us to capture high-quality grocery-anchored centers that will enhance cash flow and value to our Fund.

We reconfirmed our commitment to California’s urban real estate markets by selecting four investment partners to invest \$200 million in the development of real estate projects in California urban settings. The investments, part of CalPERS California Urban Real Estate Initiatives program, harness the investment opportunities created by the growth of California’s population and the shortage of general development in the State’s urban locations. The partners we selected focus on the development and redevelopment of multi-family units, single family housing, industrial, office, and mixed-use property types in urban settings. They included \$60 million to Buchanan Street Partners, Inc., \$60 million to Capri/Capital Advisors, LLC, \$40 million to Institutional Housing Partners, Inc., and \$40 million to American CityVista Ltd.

a closer look at
Real Estate
(Dollars in Billions)

Core Portfolio	Market Value
Office	\$3.1
Industrial	2.8
Retail	2.2
Apartment	1.1
Total Core Portfolio	\$10.2
Specialized Real Estate Portfolio (housing, timber, California urban infill)	\$2.7
Total Real Estate	\$12.9

We also made a \$125 million investment into CIM California Urban Real Estate Fund, L.P., an investment fund managed by the real estate firm CIM Group, LLC. The Fund targets investments in commercial and residential real estate projects in urban areas throughout California. CIM has an impressive resume of transactions that includes work with local community redevelopment agencies and city developers. CIM has redeveloped sites in San Diego's Gaslamp District, Old Town Pasadena, and Santa Monica's Third Street Promenade. Future California development projects include downtown San Diego and Old Downtown in Brea.

The convergence of California's technology and real estate industries and the energy crisis in California offered CalPERS a unique opportunity during the year to invest in companies that develop real estate technology infrastructure and services, and in real estate assets expected to benefit from providing space or services to tenants in high-growth sectors of the economy.

We made a \$15 million investment in a company that provides the most valuable amenity in California's crisis—low-cost energy. The company, RealEnergy, has created the largest commercial solar power system in the Western Hemisphere.

RealEnergy relies on photovoltaic power—essentially on-site energy systems such as solar, microturbine, natural gas engines, and other “green” power alternatives—deployed to generate electricity and heat that displaces power from central plants that otherwise would be consumed during peak daytime hours. Peak-hour electricity from our nation's power grid is the most expensive, and most vulnerable to spikes, surges, brownouts, and blackouts.

In a show of confidence in our investment, we teamed up with one of our real estate partners and RealEnergy to install almost an acre of advanced photovoltaic panels that sit atop three Southern California industrial buildings. The project included Carlsbad Pointe, a 320,000 square-foot industrial property owned by CalPERS.

As an investor in California real estate, we believe the advent of office buildings using their own electricity offer us many benefits. For tenants of our building, it provides a hedge against an unstable energy market. It increases the reliability of power systems and minimizes the risk of power outages. This is especially important to today's high-technology corporations.

Global Public Markets

It was a volatile year in the public markets as most investors gave back some of the superior returns earned in the stock market in recent years. Although the market volatility appeared dramatic when it occurred, we fully anticipated these moments in our asset allocation process, and to a lesser extent, looked for bargains in the market.

On the international front, we selected 14 investment firms to actively manage between \$6 to \$11 billion of the our international equity assets. The lineup of investment firms included 10 international equity managers, three Pacific Basin managers, and one Japan manager selected from a world-wide search. We are confident that we have found a stable of managers that exemplify some of the best investment expertise needed to manage the complexity of the international equity markets.

The CalPERS Board also established a \$1 billion hedge fund program and tapped Blackstone Alternative Asset Management as its strategic advisor. Hedge funds employ alternative investment strategies that allow the fund manager to invest in both long- and short-term investments. Our program will target funds that take equity exposure while limiting the amount of credit exposure. We have made a commitment to

invest cautiously, intelligently, and prudently in the hedge fund market, and expect to make 10 to 15 hedge fund investments, each between \$50 and \$100 million. Our focus will be conservative, experienced hedge fund managers who can add value to the CalPERS portfolio while not taking on additional risk or leverage. We believe CalPERS has an important role in helping to shape the hedge fund market.

Additionally, we added five new managers to our innovative program that focuses on the development of new and emerging money managers. Through our program partners Strategic Investment Management and Progress Putnam Lovell Advisors, LLC, we hired Golden Capital Management, Broadmark Asset Management, Shenandoah Asset Management, Philippe Asset Management, and Denali Advisors. We allocated more than \$600 million in international and U.S. assets and took minority equity stakes in each firm. With CalPERS assets and capital, these firms are expected to receive the support and assistance they need to become significant players in the institutional marketplace. As these firms grow and mature, we will realize profits from our equity position and returns on our investment portfolio.

In an unprecedented decision, the CalPERS Board voted to sell our \$525 million in primary tobacco holdings during the year. The action followed months of debate and testimony on the economic effects of divestment. We took the action because of the unusual and unique situation that the tobacco industry faces. We believed the large amount of legal, regulatory, and legislative action in the industry could substantially reduce our shareholder value in tobacco, and the action was taken to protect our members' assets in the long term.

We consider primary tobacco holdings to be those companies that are directly involved in the manufacture of tobacco products, including industry giants such as Philip Morris, Loews Corp., and British American Tobacco. Our decision means that we will have tobacco-free indices and benchmarks for all of our passively-managed investments. Approximately \$365 million of our tobacco holdings is held in U.S. portfolios that are managed for the defined benefit plan, Legislators' Retirement Fund, Volunteer Firefighters' Fund, Judges' I and Judges' II Retirement Systems, Supplemental Contributions Program, and Long-Term Care Program. More than \$158 million is in international tobacco holdings. In total, our tobacco stocks represent less than 1 percent of the System's passively-managed equity and fixed income investments.

And once again, we issued our "Focus List" of Corporate America's poorest performers. The companies included Warnaco, Circuit City, Lance, Metromedia, and Ralcorp. CalPERS pushed a variety of corporate governance improvements at these companies in an effort to generate better returns and long-term performance. Several companies agreed to corporate governance changes, including electing independent directors, appointing lead independent directors, conducting board self-evaluations, and adding independent directors to their audit, compensation, and nominating committees.

California Investments

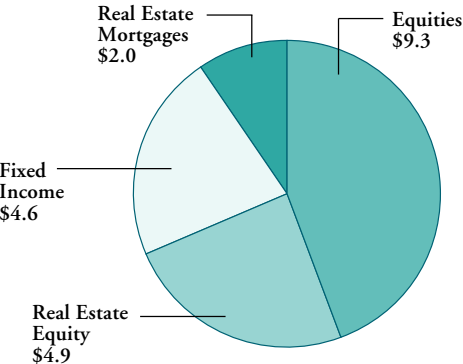
CalPERS investments have been a critical part of the economic fabric of California since the early 1980s, and our California investment portfolio has grown steadily over the last five years. As of June 30, 2001, approximately 13.4 percent—or \$20.9 billion—of our \$156 billion Fund was invested or earmarked for investment in California.

California investments are part of each asset class in our investment portfolio and are expected to deliver a return commensurate with similar investments of comparable risk. The CalPERS Board considers California investments and all other investments on the sole basis of investment merit. Investments must be financially comparable to other available investment alternatives.

Investments in California may have the ancillary benefit of creating jobs, housing, and improvements to the general infrastructure and, more importantly, serving the broad interests of CalPERS members. By strengthening the State’s economy and the well-being of our employers, our California investments help promote the continued ability of employers to make contributions to the System.

Today we invest more than \$9 billion in companies that make their home in California. These include established publicly-traded corporations and young entrepreneurial businesses that rely on CalPERS private placement capital for growth and expansion. Our fixed income assets, largely held in corporate bonds, total approximately \$766 million. We are one of the largest California real estate developers, financing more than \$5 billion worth of single family homes and general real estate holdings. In fact, CalPERS has committed \$40 million to invest in senior housing throughout the State. And our Member Home Loan Program, implemented in 1989, has provided nearly \$10 billion in mortgages to nearly 71,000 California families.

CalPERS
California Investments
Market Value
\$20.8 Billion
(Dollars in Billions)





The 2001 State Legislative Year

The following is a brief summary of some of the CalPERS-related legislation enacted during the first year of the 2001-02 Session of the California Legislature. (New laws become effective January 1, 2002, unless otherwise noted.)

A.B. 616, Chapter 782 (Calderon)

Authorizes local contracting agencies to provide three new retirement formulas for local miscellaneous members with a member contribution rate of 8 percent of compensation, subject to contract amendment. The formulas begin at 2% at 50 and increase incrementally up to 2.5% at 55, 2.7% at 55, and 3% at 60. Includes similar provisions for 1937 Act County Retirement Systems.

A.B. 824, Chapter 185 (Cohn)

Authorizes the CalPERS Long-Term Care Program to accept the enrollment of siblings of active and retired public employees currently eligible to enroll in the Program.

A.B. 1099, Chapter 433 (Havice)

Permits members of the Judges' Retirement System (JRS) and Judges' Retirement System II (JRS II) to purchase service as a subordinate judicial officer prior to becoming a judge, if the member pays the actuarial present value of the increase in benefits due to the additional service, excluding service credited to another retirement system. Adds provisions for the monthly allowance of a judge who elects an optional settlement at retirement to revert (or "pop up") to the unmodified allowance amount if the retired judge's spouse predeceases the judge. Authorizes JRS and JRS II members to participate in the Supplemental Contributions Program. Includes JRS II among the systems that have reciprocity for final compensation.

S.B. 90, Chapter 796 (Dunn)

Increases the retirement benefit limit from 85 percent to 90 percent of final compensation for local safety members who retire on or after January 1, 2002.

S.B. 165, Chapter 77 (O'Connell)

Permits any member of CalPERS who is subsequently employed to perform service subject to coverage by the CalSTRS Defined Benefit Program to elect to retain coverage under CalPERS for that service. All local members and most State members would be required to have at least five years of credited service in CalPERS to be eligible to make this election.

S.C.R. 15, Resolution Chapter 140 (Soto)

Encourages establishment of an appropriate system to annually determine a minimum standard of pension adequacy for all retired members of CalPERS, to identify funding resources for annually adjusting retired members' pensions to maintain that minimum standard, and to identify extraordinary earnings of the Retirement Fund in excess of prudent reserves for the purpose of enhancing retired members' pensions. (Effective September 26, 2001.)

*S.C.R. 39, Resolution
Chapter 142 (Soto)*

Establishes a panel to study the pharmacy benefits, copayments, and benefit structure of the PEMHCA (Public Employees' Medical and Hospital Care Act) program, with recommendations due to the Legislature by March 1, 2002, and a final report due by June 1, 2002. (Effective September 26, 2001.)

Federal Update

Our federal relations program continued to ensure that the interests of the System, our members, and employers were addressed in the overall federal policymaking process during the 2000-01 fiscal year. CalPERS was involved in federal initiatives covering a variety of pension and health benefit matters.

Legislation to improve the flexibility of pension plans was signed into law on June 7, 2001. Starting in 2002, it will improve portability of pension assets by allowing rollovers of retirement benefits among various types of deferred compensation and defined contribution plans (457, 403(b), and 401(k) plans, and certain types of IRAs) when employees switch jobs. The law will also allow assets from all deferred compensation and defined contribution plans to be transferred or rolled into defined benefit plans to assist employees who want to purchase service credit.

Social Security program reform has continued to be a top priority in Washington, with attention focused on the President's Commission to Preserve Social Security created in May 2001. The Commission held

a public hearing in San Diego in September 2001, where several witnesses brought up the issue of mandatory Social Security coverage of all newly hired State and local government employees. Congressional legislation has been delayed pending the findings of the Commission, which are tentatively scheduled for release in late 2001.

The growing awareness of the rising costs for prescription drugs, especially for the elderly, continues to be a major health care issue for Congress and the White House. The dilemma is how to structure a Medicare prescription drug benefit that provides meaningful relief for seniors while staying within federal budget limits. Other approaches to skyrocketing drug prices propose to improve the process for getting generic drugs on the market and to allow certain U.S.-manufactured drugs sold overseas to be reimported at lower prices than medicines sold domestically.

While enjoying strong support in Congress, legislation to make long-term care more affordable may not see action until 2002. Under the latest proposal, long-term care insurance expenses could become fully deductible. Another proposal would offer new tax credits to family caregivers.

Federal legislation that could save investors an estimated \$14 billion over the next decade is close to final passage. The proposal would reduce regulatory fees paid by investors, including CalPERS, and provide the Securities and Exchange Commission greater flexibility in paying its employees by providing so-called “pay parity” with other financial regulators. This could help stem the high staff turnover rate and provide regulatory stability. In February 2001, CalPERS Chief Executive Officer Jim Burton testified in support of the Senate bill at a Senate Banking Committee hearing.

Bankruptcy reform is another proposal that is close to final passage. The bill would expand pension protections for public plan participants in the event of their individual bankruptcy and would ensure that ongoing plan contributions would be allowed.


Fiscal year 2001-02 will be the 71st year since our founding. Our goal is the same today as when CalPERS opened our doors in January of 1932: to provide quality service, effectively and efficiently manage benefits, and prudently manage assets.

In the coming year, we will press on to achieve measurable improvements in customer service and education. We will focus on improving timeliness and quality of direct customer service, and we will continue to provide a robust variety of methods for members and employers to conduct business with us—whether they wish to call, write, visit, or connect via the Internet. Next year we will complete requirements for the Member Benefit Contact Center and will also phase-in three web-based member self-service projects. By the end of next fiscal year, members will be able to go on-line to order forms and publications, register for seminars, and

request retirement estimates. A new on-line change of address program will follow in late 2002 or early 2003.

Our plans in the area of asset management are ambitious as well. We're going to implement some of the latest technology solutions to enhance our asset management performance. For example, we'll continue our work toward Straight Through Investment Transaction Processing (STP), which will enable our investment staff to settle trades in one business day, rather than the current three. STP will be executed through a five-phased process. The first three, developing a strategy, assessing current capabilities, and developing a future automated operation model that is capable of settling trades in one business day have already been completed. Phases four and five will involve evaluating alternative solutions for the model, and procuring systems and software to meet our business needs. Our goal is to implement STP by June 2004.

Work will continue on our integrated corporate database, COMET, the CalPERS On-Line Member and Employer Transaction system. The February 2002 launch of three COMET systems—member registration, employer contracts, and State employee appointment transactions will be one of the



largest system implementations in CalPERS history, involving the training of more than 700 employees. When finalized, COMET will replace several existing CalPERS systems, including member and employer registration, employee appointments, contribution reporting, and employer reserves, and will allow faster and more accurate processing and retrieval of data.

We have embarked on a member records imaging system and will complete this project during fiscal year 2001-02. The system will digitally store and retrieve critical member files, improving yet another tool we use to administer benefits.

We will continue to press our health providers for quality health care at a reasonable cost, work to keep our self-funded plans on a stable course, and work on innovative long-range strategies for managing in this most challenging era in health care management.

We are encouraged by the strong support we receive from our members. Our latest member survey gives CalPERS high marks. Of the 1,100 State, public agency, and school members polled, 83 percent believe we are financially strong; 88 percent are confident that their retirement money will

be there for them when they need it, and 84 percent are satisfied with our service. We are grateful for member confidence in us, but recognize that we must continuously improve to meet their changing expectations.

We look forward to the year ahead and to continuing our mission of providing retirement and health security to all those we serve.



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